

## Message Text

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SUBJ: SPANISH BALANCE OF PAYMENTS

1. SUMMARY: SPAIN'S BALANCE OF PAYMENTS SITUATION IS NOW VIEWED IN GOS AS MOST IMPORTANT AND MOST IMMEDIATE ECONOMIC PROBLEM FACING COUNTRY. CONTINUED HIGH LEVEL OF IMPORTS AND FAILURE OF EXPORTS TO INCREASE AS MUCH AS HAD BEEN HOPED HAVE INCREASED TRADE DEFICIT BY 22 PER CENT IN FIRST FIVE MONTHS AND CAUSED \$400 MILLION DECLINE IN RESERVES DESPITE HIGHER RECEIPTS FROM TOURISM AND EMIGRANT WORKERS AND OFFICIAL BORROWINGS ABROAD OF OVER \$550 MILLION. OUT-LOOK FOR 1975 IS CURRENT ACCOUNT DEFICIT OF SOME \$3 BILLION AND YEAR-END RESERVES SLIGHTLY ABOVE \$5 BILLION. GOS WILL PROBABLY GO ALONG WITH PRESENT SITUATION FOR AT LEAST A FEW MORE MONTHS. SUMMER TOURIST RECEIPTS SHOULD HELP RESERVES, AND REDUCED ECONOMIC ACTIVITY SHOULD AT LAST BEGIN TO DAMPEN IMPORTS. MOST IMPORTANTLY SPAIN IS WATCHING FOR PICK UP IN EXPORTS AS ECONOMIES OF HER MAJOR TRADING PARTNERS REVIVE, BUT IF THIS FAILS TO COCURE WITH SUFFICIENT STRENGTH, GOS MAY RESORT TO MORE SEVERE MEASURES AIMED AT RESTRICTING IMPORTS AND PRESERVING A STILL COMFORTABLE LEVEL OF RESERVES. END  
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SUMMARY.

2. GENERAL DETERIORATION OF SPAIN'S BALANCE OF PAYMENTS PICTURE THROUGH FIRST FIVE MONTHS OF 1975 HAS BECOME OF INCREASING CONCERN TO GOS WHICH IS NOW FOCUSING ATTENTION MORE ON THIS AND RELATED HIGH RATE OF INFLATION THAN ON GROWTH LEVELS AND UNEMPLOYMENT AS WAS TRUE FROM MID 1974 (WHEN OIL CRISIS FIRST BEGAN TO BE FELT HERE) TO BEGINNING OF 1975. QUANTITATIVE FORECASTS OF 1975 BALANCE OF PAYMENTS ARE EXCEEDINGLY DIFFICULT, BUT AT THIS POINT THERE IS REASON TO BELIEVE THAT CURRENT ACCOUNT DEFICIT WILL MATCH OR EVEN EXCEED RECORD \$3.1 BILLION LEVEL OF 1974. IT IS UNLIKELY THAT IT WILL DROP MUCH BELOW THAT LEVEL, AND WITH FOREIGN INVESTMENT IN SPAIN BELOW 1974 FIGURE, GOS IS BEING FORCED TO BORROW MORE ABROAD AND WILL HAVE TO DRAW RESERVES DOWN BY AT LEAST THE \$600 MILLION FIGURE OF 1974.

3. SPANISH IMPORTS (CIF) THROUGH MAY WERE UP 21 PERCENT TO \$7.2 BILLION (VS. \$5.9 BILLION IN 1974); EXPORTS (FOB) ROSE 20 PERCENT TO \$3.3 BILLION FROM \$2.8 BILLION LEAVING TRADE DEFICIT OF \$3.9 BILLION, 22 PERCENT ABOVE SAME PERIOD IN 1974. WITH EXCEPTION OF APRIL, WHEN IMPORTS HIT RECORD \$1.6 BILLION, THEY HAVE BEEN RATHER STEADY AT \$1.3 TO \$1.4 BILLION, MORE OR LESS COMPARABLE TO LEVELS REACHED IN FINAL SEVEN MONTHS OF 1974. EXPORTS HAVE BEEN DISAPPOINTING, HURT PARTLY BY HIGH SPANISH INFLATION BUT MAINLY BY DECLINE IN DEMAND ABROAD. TRADE OUTLOOK FOR 1975 REMAINS HIGHLY UNCERTAIN. EXPECTATION OF SOME SLOWDOWN IN IMPORTS DUE TO DECLINE IN DOMESTIC DEMAND AND DEPRECIATION OF PESETA AGAINST EUROPEAN CURRENCIES SEEMS REASONABLE ENOUGH ALTHOUGH SPANISH IMPORT DEMAND IS RATHER INELASTIC. IMPORTS ARE LARGELY RAW MATERIALS, ESPECIALLY PETROLEUM, CAPITAL EQUIPMENT, AND ESSENTIAL FOODSTUFFS. PETROLEUM IMPORTS (CIF) FOR FIRST QUARTER 1975 WERE \$884 MILLION OR 21.3 PERCENT OF TOTAL IMPORTS. THIS COMPARES WITH \$524 MILLION AND 16.1 PERCENT IN FIRST QUARTER 1974 AND \$225 MILLION AND 10.2 PERCENT IN FIRST QUARTER 1973. FOR 1974 AS A WHOLE PETROLEUM IMPORTS OF \$3.5 BILLION COMPOSED 22.3 PERCENT OF TOTAL IMPORTS. WITH ECONOMY CONTINUING TO SHOW SOME GROWTH, EVEN THOUGH REDUCED TO 2 TO 3 PERCENT FROM 5 PERCENT LEVEL OF 1974, DEMAND FOR IMPORTS CAN BE EXPECTED TO CONTINUE SUFFICIENTLY STRONG LIMITED OFFICIAL USE

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SO THAT NO LARGE OR SUDDEN DROP IS LIKELY.

4. GOS HAS BEEN EMPHASIZING NEED TO PUSH EXPORTS RATHER THAN ARTIFICIALLY RESTRICT IMPORTS. WHILE EXPORTS ARE WELL ABOVE COMPARABLE 1974 PERIOD, THIS TO LARGE EXTENT REFLECTS HIGHER PRICES (AS IS ALSO TRUE WITH IMPORTS), AND COMPARED WITH LAST 4 MONTHS OF 1974, WHEN EXPORTS JUMPED CONSIDERABLY, FIVE-MONTH PERFORMANCE FOR 1975 REPRESENTS AVERAGE MONTHLY

DECLINE OF 5.7 PERCENT. SOME SPANISH OFFICIALS ARE EXPRESSING INCREASING DOUBT THAT REVIVAL OF ECONOMIES OF MAJOR TRADING PARTNERS, PARTICULARLY WEST GERMANY AND US, WILL OCCUR SOON ENOUGH TO HELP SPANISH SITUATION. (MINFIN OFFICIAL IN PRIVATE RECENTLY HAD PARTICULARLY SCATHING WORDS FOR FRG ECONOMIC POLICY.) IN SUCH A CASE GOS MAY FEEL JUSTIFIED IN IMPLEMENTING SOME FORM OF IMPORT RESTRICTIONS, DESPITE CONTINUING RELATIVELY HIGH RESERVESS.

5. TRADE DEFICIT (FOB/FOB) FOR 1975 IS EXPECTED TO BE CLOSE TO \$7 BILLION FIGURE IN 1974, BUT ESTIMATE IS BASED ON CONSIDERABLE UNCERTAINTY OVER BOTH IMPORT AND EXPORT BEHAVIOR DURING REST OF THIS YEAR. PROJECTIONS BASED ON PAST YEARS ARE LITTLE HELP, BUT IT IS PROBABLY FAIR TO SAY THAT ANY MAJOR DEVIATION FROM \$7 BILLION ESTIMATE WILL BE TOWARD LARGER RATHER THAN SMALLER DEFICIT. FOB EXPORT FIGURES FOR 1975 NOT AT PRESENT AVAILABLE BUT ON CIF/FOB BASIS TRADE DEFICIT OF \$3.9 BILLION IN FIRST FIVE MONTHS IS ALREADY \$700 MILLION ABOVE MAY 1974 LEVEL AND COULD GO HIGHER BEFORE TURNING DOWNWARD, ALTHOUGH DEFICIT FOR MAY 1975 WAS \$8 MILLIN BELOW MAY 1974.

6. BOTH RECEIPTS FROM TOURISM AND REMITTANCES FROM EMIGRANT WORKERS HAVE BEEN SURPRISINGLY GOOD THIS YEAR, AND TOURIST BOOKINGS FOR THE SUMMER, WHEN SOME 40 PERCENT OF ANNUAL TOURIST RECEIPTS ARE NORMALLY REALIZED, ARE STRONG. REFLECTING HIGHER PRICES, TOURIST RECEIPTS THROUGH APRIL WERE ESTIMATED AT \$824.9 MILLION, 11 PERCENT OVER 1974 DESPITE A 14.3 PERCENT DECLINE IN THE NUMBER OF VISITORS. WORKERS REMITTANCES HAVE BEEN CONSIDERABLY HIGHER IN 1975 DESPITE INCREASED UNEMPLOYMENT IN EUROPE, POSSIBLY REFLECTING REPATRIATION OF SAVINGS BY RETURNEES OR PERHAPS BELIEF BY EMIGRANTS THAT CURRENCIES SUCH AS FRENCH FRANC AND DM HAVE LIMITED OFFICIAL USE

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REACHED PEAK AGAINST PESETA. PRIVATE TRANSFERS, OF WHICH SOME 60 PERCENT IS FROM EMIGRANT WORKER REMITTANCES, WERE \$306 MILLION THROUGH MARCH, 44PERCENT OVER 1974.

7. FOREIGN INVESTMENT OUTLOOK IS LESS SANGUINE IN SHORT TERM, IN PART BECAUSE OF WORLD ECONOMIC SITUATION IN GENERAL, AND IN PART BECAUSE O F UNCERTAINTY OVER FUTURE POLITICAL SITUATION IN SPAIN. HERE SPAIN APPEARS TO BE SUFFERING SOME FALLOUT FROM PORTUGAL. LONG TERM PRIVATE CAPITAL INFLOWS IN FIRST QUARTER DECLINED TO \$67 MILLION IN 1975 FROM \$220 MILLION IN 1974. WHILE THIS REPRESENTS TOO SHORT A PERIOD TO DRAW ANY CONCLUSIONS, GOS OFFICIALS REPORT A VERY DEFINITE DECLINE IN FOREIGN INVESTMENT IN FIRST FIVE MONTHS ALTHOUGH THEY VELIEVE THERE MAY BE SOME IMPROVEMENT DURING SECOND HALF OF THIS YEAR.

8. AT END OF MAY RESERVES WERE PROVISIONALLY \$5.639 BILLION, A DECLINE OF \$364 MILLION SINCE JAN 1. (HIGH POINT FOR SPANISH RESERVES WAS \$6.768 BILLION IN DECEMBER 1973.) DECLINE IN RESERVES THIS YEAR HAS BEEN LIMITED BY OFFICIAL BORROWING, IN PARTICULAR \$372 MILLION LOAN IN MARCH UNDER 1974 AUTHORIZATION OF IMF OIL FACILITY. VIRTUALLY ALL OF THIS COULD BE SAID TO HAVE GONE FOR \$360 MILLION INCREASES IN PETROLEUM IMPORTS IN FIRST QUARTER. BANK OF SPAIN FIGURES FOR FIRST QUARTER 1975 LIST TOTAL OFFICIAL PUBLIC CREDITS OF \$584 MILLION (VS. 1974 FIGURE OF \$26 MILLION), WHICH INCLUDES OIL FACILITY PLUS, LARGELY, BORROWINGS BY RENFE, THE NATIONAL RAILROAD. ADDITIONAL LOANS BY THE TELEPHONE COMPANY AND THE NATIONAL CREDIT INSTITUTE WILL HELP MAINTAIN RESERVE LEVEL AS WILL 1975 OIL FACILITY AUTHORIZATION OF SOME \$660 MILLION WHICH SPAIN IS EXPECTED TO UTILIZE. FOREIGN BORROWING IS THUS KEY TO MAINTENANCE OF ACCEPTABLE RESERVE LEVEL FOR THIS YEAR AND PROBABLY FOR MUCH, IF NOT ALL, OF 1976 AS GOS ATTEMPTS TO IMPROVE TRADE SITUATION THROUGH MODERATELY RESTRICTIVE DOMESTIC POLICY WHILE WAITING FOR FOREIGN DEMAND TO RECOVER.

9. IMPROVEMENT IN RESERVES FROM SUMMER TOURIST RECEIPTS COUPLED WITH EXPECTED SOFTENING OF IMPORT DEMAND PROBABLY PERMITS GOS AT LEAST A 3 TO 4 MONTH BREATHING SPACE. IN ANY EVENT, FINANCING OF 1975 DEBT SEEMS TO LIMITED OFFICIAL USE

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PRESENT NO MAJOR PROBLEMS, DESPITE REPORTS THAT SOME RECENT SPANISH DEBT ISSUES HAVE NOT PROVEN PARTICULARLY ATTRACTIVE TO INTERNATIONAL LENDERS. WITH HIGH RESERVES SPAIN STILL HAS ROOM TO MANEUVER, BUT AS ONE FINANCE OFFICIAL NOTED, SPAIN IS WALKING A TIGHTROPE AND NEEDS TO GET CURRENT ACCOUNT DEFICIT DOWN TO ANNUAL RATE OF ABOUT \$2.5 BILLION BY END OF THIS YEAR IF SHE IS TO MAINTAIN THE SAME HIGH CREDITWORTHINESS IN 1976 AS IN RECENT YEARS. WITH PICTURE FOR 1975 AS A WHOLE EXPECTED TO BE NO BETTER- AND PROBABLY SOMEWHAT WORSE - THAN 1974, THIS POSES A SUBSTANTIAL PROBLEM FOR REMAINDER OF THIS YEAR.

10. IN DISCUSSIONS WITH GOS OFFICIALS, EMBASSY WILL CONTINUE TO ATTEMPT TO DISCOURAGE ANY FORM OF IMPORT RESTRICTIONS. STABLER

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